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8602.00/8-1960

FROM : Amembassy HELSINKI

89

DESP. NO.

TO : THE DEPARTMENT OF STATE, WASHINGTON

August 19, 1960

DATE

REF : CERP Section C, Item 3

EUR INDEX
WRC

AUG 19 1960

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SUBJECT: Finland - Interim Economic Assessment

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SUMMARY

As predicted earlier this year, the status of the Finnish economy has continued to improve rapidly, with production up in practically every sector, investment programs well under way and unemployment disappearing. Government finances are in good shape now because of higher revenues, but budget makers can be expected to raise expenditures for next year. Renewal of farm income legislation threatens to become a subject of controversy this fall.

Although rising imports are a constant threat to foreign exchange reserves, Finland's foreign trade position is developing satisfactorily and should continue to do so during the remainder of the year. Trade with the United States is up sharply and liberalization of dollar imports has created new opportunities for sales of U.S. goods to Finland.

There have been no very significant developments in Finland's economic relations with the Soviet Bloc, except that concern over the Soviet attitude has continued to impede Finnish action on EFTA affiliation. Caution is still the byword in matters concerning the Bloc, particularly as international tensions have mounted.

Domestic Economy

Nothing has occurred in the last six months to warrant changing the overall views on the status of the Finnish economy expressed in the Comprehensive Economic Assessment (D-597, February 24, 1960). Production has continued to increase along the general lines indicated, with the industrial sector operating about 15% above last year's level. Particularly impressive has been the performance of the construction industry, where increases in commercial and industrial construction have contributed significantly to the current revival. The upward trend as a whole has accelerated somewhat faster than originally estimated, and investment programs have gone forward rapidly. Finnish officials are now predicting that net national product in real terms will rise 7% and national income 6-7% over last year's level.

The present boom, bolstered by active investment programs and a high level of exports, should continue into 1961. Beyond then it is impossible to predict with certainty, because domestic conditions depend to such a degree on demand for Finnish

EV Youngquist/mh
REPORTER

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products in western Europe. All signs point to the next six months as a critical period. After that it may be possible to see more clearly how economic developments in Europe are shaping up and appraise Finland's chances of obtaining capital for further economic expansion.

As predicted, unemployment fell sharply during the year, and reached a low early this summer when all unemployment registers closed for the first time since 1956. Unemployment during the coming months should remain much below the level of recent years, according to official estimates, because of active timber felling programs for the coming winter. These will benefit directly the small farmers who need work during the winter and usually constitute almost 80% of registered unemployed. Thus far the price level in Finland has not given cause for concern, although the upward pressures previously noted still exist and bear watching. Prices have risen only fractionally during recent months, and a total rise of about 3% is forecast for the entire year.

As expected, the annual adjustment of farm income according to the Farm Income Law will result in a minimal increase in prices of some agricultural products. It appears increasingly likely that the question of new farm income legislation will be a basis of major political controversy this fall. The present law covers only the coming crop year, and a heated battle is expected when the Agrarians introduce substitute legislation during the forthcoming session. Other parties, in particular the Social Democrats, will oppose vigorously any arrangement which in their view grants excessive benefits to the farm sector.

The government's fiscal position has been favorable so far this year, benefiting from tax receipts substantially in excess of budget estimates. This happy state should continue until the end of the year. Next year's budget is now being discussed among the ministries and the Government is rushing preparation of its budget proposal. According to preliminary estimates, the proposed figure for expenditures will be significantly above the level of the basic budget for this year. In all likelihood, the expenditure side of the budget will be increased even more when it is considered by the parliament; political pressures, plus the inviting prospect of higher revenues, almost certainly will lead to further inflation of expenditures. Thus the possibility pointed out earlier - that expenditure plans based on higher income may run afoul of lower receipts in case of a slowdown in economic activity - will remain as a threat to the Government's fiscal situation. The final totals for the 1961 budget will not be established until the parliament is well into the fall session.

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The general situation in investment has not altered materially since the Embassy's assessment earlier this year. While sufficient funds are available for current projects, there is still a need for additional long-term capital in the future. Because of the limited ability of the Finnish economy to provide these funds, foreign capital will be needed. No changes have taken place yet in Finland's investment climate to overcome the geo-political factors inhibiting foreign private investment here, which means that Finland must look to international or foreign government or

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quasi-government sources for substantial loan assistance. So far as the Embassy knows no progress has been made toward obtaining funds from these sources additional to those already programmed, although the International Bank has been asked to give preliminary consideration to a further credit for development of the woodprocessing industry. Prospects for a Swiss bank loan, which has been under discussion periodically, do not appear good for the present.

Foreign Economic Relations - END CONFIDENTIAL - BEGIN UNCLASSIFIED

As indicated in the Embassy's earlier assessment, the chief danger to Finland's foreign exchange reserves is the rising level of imports as a result of the domestic economic upswing. Exports have increased substantially this year, but they have been far outstripped by imports. As a consequence, Finland's first six months trade figures show a sizable deficit (Fmk 34.7 billion vs Fmk 7.6 billion for January - June last year). The export season is now in full swing, however, and imports have begun to return to a more normal level, supporting the view that trade for the year will not result in an unmanageable deficit. Current estimates for the full year place both exports and imports at all-time highs, with a trade deficit of about Fmk 22 billion, partially offset by a favorable balance of about Fmk 12 billion in invisibles. Despite the heavy import surplus, it is expected that Finland's foreign exchange position will continue relatively strong for the entire year, because a large portion of the imports of investment goods have been purchased on medium or long-term credit.

Trade between Finland and the United States has developed in general along the lines predicted earlier. As a result of the liberalization of dollar imports coupled with generally high import demand this year, U.S. exports to Finland in the first four months more than doubled last year's figures, surpassing the most optimistic expectations at the beginning of the year.

As expected, most of the improvement has been noted in exports of machinery. U.S. manufacturers are participating heavily in the expansion program of the Finnish pulp and paper industry, and Finland's imports of U.S. industrial machinery and equipment make up about half of total imports from the United States. Judging from the sharp increase in the number of local trade inquiries received by the Embassy since the liberalization, there seems to be considerable interest in purchasing U.S. products. U.S. goods generally have a reputation for durability and high quality, and the Embassy feels that there are real opportunities for expansion of the American market in Finland, particularly in consumer goods.

Finland's sales to the United States are increasing also, but, as indicated earlier this year, consist primarily of traditional exports such as newsprint and other pulp and paper products. Finland continues to work toward exporting more of its secondary products to the United States, and has had considerable success in introduction of particular items such as sporting weapons, pleasure boats, and art glass. The dollar value and economic significance of these remain minimal, however, in comparison with the traditional wood product exports.

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there have been no very important developments in Finnish-Soviet economic relations. Trade with the Soviet Union as a percentage of total trade has nearly held its own and the increase in both imports and exports has led to a supplementary trade agreement with the USSR for 1960. This agreement adds about 5% to trade in each direction. This is less than the increase in trade with the West for the same period, but does not mean any real diminution of the Soviet position because the ups and downs in Finnish trade with the USSR usually lag somewhat behind the trend of trade with the world as a whole.

Arrangements have been completed for use of the Soviet ruble credit by private borrowers and decisions on a number of possible uses are expected soon, but there has been only one minor purchase to date and it is still too early to tell the extent or specific nature of the effects of the credit. Purchases of rails for the State Railways and blast furnace equipment for the newly-formed State-owned iron and steel company appear likely.

For the Ambassador:

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